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FORM 10-Q
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

☒ [X] QUARTERLY REPORT UNDER SECTION 13 OR 15 (d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended June 30, 1992

☐ [] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 0-15935

ALPHABEL INC.
(Exact name of registrant as specified in its charter)

CALIFORNIA
(State or other jurisdiction of
incorporation or organization)

95-3634089
(I.R.S. Employer
Identification No.)

3601 CALLE TECATE, CAMARILLO, CA 93012
(Address of principal executive offices and zip code)

(805) 482-9815
(Registrants telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES X NO

Number of shares of Common Stock outstanding
at July 31, 1992: 11,350,831

Number of Sequentially Numbered Pages: 12
Exhibit Index at Page 11

ALPHAREL INC.

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ALPHAREL, INC.

PART I. FINANCIAL INFORMATION

CONSOLIDATED BALANCE SHEETASSETS

	June 30, 1992 (unaudited)	December 31, 1991
Current assets:		
Cash and cash equivalents	\$ 4,569,000	\$ 4,724,000
Receivables	1,372,000	1,004,000
Inventory	1,163,000	1,062,000
Other current assets	<u>167,000</u>	<u>79,000</u>
Total current assets	7,271,000	6,869,000
Property and equipment, net	615,000	686,000
DDTMS technology, net	1,680,000	1,992,000
Computer software, net	251,000	63,000
Other assets	<u>396,000</u>	<u>452,000</u>
Total assets	<u>\$10,413,000</u>	<u>\$10,062,000</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Current portion of capital lease obligations	\$ 81,000	\$ 117,000
Current portion of note payable	111,000	106,000
Accounts payable	600,000	222,000
Accrued liabilities	228,000	681,000
Billings in excess of costs	<u>45,000</u>	<u>13,000</u>
Total current liabilities	1,065,000	1,139,000
Capital lease obligations	127,000	169,000
Note payable	<u>203,000</u>	<u>260,000</u>
Total liabilities	1,395,000	1,568,000
Commitments and contingencies		
Shareholders' equity:		
Common stock, 20,000,000 shares authorized; 11,350,831 and 11,026,631 issued and outstanding, respectively	39,134,000	38,732,000
Retained earnings (deficit)	<u>(30,116,000)</u>	<u>(30,238,000)</u>
Total shareholders' equity	<u>9,018,000</u>	<u>8,494,000</u>
Total liabilities and shareholders' equity	<u>\$10,413,000</u>	<u>\$10,062,000</u>

See accompanying notes to the consolidated financial statements.

ALPHAREL, INC.

CONSOLIDATED STATEMENT OF OPERATIONS

(Unaudited)

(In thousands except per share data)

	For the three months ended June 30,		For the six months ended June 30,	
	1992	1991	1992	1991
Revenue	\$1,394	\$1,488	\$2,760	\$3,058
Cost of revenue	<u>951</u>	<u>705</u>	<u>1,938</u>	<u>1,598</u>
Gross profit	<u>443</u>	<u>783</u>	<u>824</u>	<u>1,458</u>
Research and development	118	312	193	467
Marketing	142	142	274	239
General and administrative	<u>147</u>	<u>167</u>	<u>293</u>	<u>330</u>
Total operating expenses	<u>407</u>	<u>621</u>	<u>760</u>	<u>1,036</u>
Income from operations	36	162	64	422
Interest and other income	42	263	96	283
Interest and other expense	<u>(17)</u>	<u>(22)</u>	<u>(38)</u>	<u>(46)</u>
Income before taxes	61	403	122	659
Provision for taxes	-	-	-	-
Net income	<u>\$ 61</u>	<u>\$ 403</u>	<u>\$ 122</u>	<u>\$ 659</u>
Net income per share	<u>\$.01</u>	<u>\$.04</u>	<u>\$.01</u>	<u>\$.07</u>
Weighted average shares outstanding	11,869	10,045	11,899	10,017

See accompanying notes to the consolidated financial statements.

ALPHAREL, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited)

	For the six months ended June 30,	
	1992	1991
Cash flow from operating activities:		
Net income	\$ 122,000	\$ 659,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	280,000	288,000
(Increase) decrease in assets:		
Receivables	(308,000)	(270,000)
Inventory	(101,000)	283,000
Other assets	(88,000)	(369,000)
Increase (decrease) in current liabilities:		
Accounts payable	378,000	48,000
Accrued liabilities	(453,000)	53,000
Billing in excess of cost	32,000	(355,000)
Net cash provided (used) by operating activities	<u>(138,000)</u>	<u>337,000</u>
Cash flows from investing activities:		
Purchases of property and equipment	(77,000)	(60,000)
Purchases of software	(86,000)	-
Computer software costs capitalized	(118,000)	(2,000)
Increase in other assets	(7,000)	-
Net cash used in investing activities	<u>(288,000)</u>	<u>(62,000)</u>
Cash flows from financing activities:		
Principal payments under capital lease obligations	(79,000)	(136,000)
Principal payments under a note payable	(52,000)	(35,000)
Proceeds from exercise of stock options	20,000	30,000
Proceeds from issuance of units	382,000	-
Net cash provided (used in) financing activities	<u>271,000</u>	<u>(141,000)</u>
Net increase (decrease) in cash and cash equivalents	(155,000)	134,000
Cash and cash equivalents at beginning of period	<u>4,724,000</u>	<u>846,000</u>
Cash and cash equivalents at end of period	<u>\$4,569,000</u>	<u>\$, 980,000</u>

See accompanying notes to the consolidated financial statements.

ALPHAREL, INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 - Basis of Presentation

The accompanying consolidated balance sheet of Alpharel, Inc. (the "Company") as of June 30, 1992 and the consolidated statement of operations and of cash flows for the three and six month periods ended June 30, 1992 and 1991 are unaudited. The consolidated financial statements and related notes have been prepared in accordance with generally accepted accounting principles applicable to interim periods. In the opinion of management, the consolidated financial statements include all adjustments necessary for a fair presentation of the financial position and the results of operations for the periods presented.

Note 2 - Net Income Per Share

Net income per share is computed on the basis of weighted average shares and common stock equivalent shares outstanding for each period presented, if dilutive.

Note 3 - Inventory

Inventory consists of components of the Company's DDMS products at various stages of completion. At June 30, 1992 the Company's reserve against excess quantities of inventory was approximately \$4,730,000.

RESULTS OF OPERATIONS

THREE AND SIX MONTHS ENDED JUNE 30, 1992 COMPARED WITH THE THREE AND SIX MONTHS ENDED JUNE, 1991.

Revenue

Revenue for the three and six months ended June 30, 1992 was \$1,394,000 and \$2,750,000, respectively, as compared to \$1,488,000 and \$3,056,000 for the three and six months ended June 30, 1991. The decrease in revenue for the three and six months is primarily due to delays in orders from Caterpillar, the result of slowdowns caused by a strike by workers at Caterpillar. The striking workers returned to work in the first part of the second quarter; however, the Company did not begin to receive orders resulting from Caterpillar's reinstatement of the system rollout until the end of June. Although the system rollout has resumed, there can be no assurance the level of activity from Caterpillar for the year will not be adversely impacted by the after effects of the strike.

For the three and six months ended June 30, 1992 revenue consisted of new system revenue of \$871,000 (62%) and \$1,490,000 (54%), respectively, and \$523,000 (38%) and \$1,270,000 (46%), respectively, related to system enhancements, expansion and maintenance. This compares to 1991 revenue of \$249,000 (17%) and \$1,369,000 (45%), respectively, in new system revenue and revenue related to system enhancements, expansion and maintenance of \$1,239,000 (83%) and \$1,687,000 (55%), respectively. Proprietary hardware sales were \$74,000 and \$299,000 in the second quarter and first six months of 1992 versus \$592,000 and \$678,000, respectively for the comparable periods a year ago. Proprietary hardware sales can fluctuate significantly on a quarterly basis based on the timing of orders by those vendors providing hardware maintenance to the Army and Air Force's imaging systems which include proprietary hardware that Alpharel had manufactured in the past. The Company is no longer producing the hardware items that comprised these sales. The Company is maintaining accounting reserves in anticipation of the obsolescence of a portion of its existing inventories. However, there can be no assurance, that the Company will be able to sell such products without incurring losses in the future. The Company expects that revenues from proprietary hardware sales will decline substantially as the Company's hardware inventories decline.

A small number of customers have typically accounted for a large percentage of the Company's annual revenue. During the first six months of 1992, three customers comprised 51%, 17% and 12% of total revenue. In the first six months of 1991, three customers accounted for 30%, 26% and 12% of total revenue. One consequence of this dependence has been that revenue can fluctuate significantly on a quarterly basis. The Company's reliance on relatively few customers could have a material adverse effect on the results of its operations, particularly in light of the current prevailing adverse general economic conditions, which have adversely affected certain industries, including automotive, aerospace and defense-related manufacturing, in which many of the Company's principal customers operate. Certain of the Company's principal customers have recently experienced losses from operations and have reduced their capital expenditures. Additionally, a significant portion of the Company's revenues has historically been derived from the sale of systems to new customers. Additional sales of new systems can be expected to reduce the Company's dependence on a relatively small number of customers by providing an increasing base of customers for expansion, enhancement and maintenance services.

Gross Profit

Gross profit as percentage of revenue was 32% and 30% for the three and six months ended June 30, 1992. For the comparable periods in 1991, gross profit percentage was 53% and 48%, respectively. The decrease in gross profit percentage in the second quarter 1992 was primarily due to the fact that a greater portion of revenue was attributable to the sale of third party hardware which has a significantly lower margin than the sale of the Company's software and services. Also contributing to the lower gross profit percentage for the first six months of 1992 versus 1991, was the sale of a third party software product in first quarter 1992. Gross profit percentage can fluctuate quarterly based on the percentage of revenues attributable to

the resale of third party software or hardware. These products are resold at a lower gross profit percentage in order for the Company to remain competitive in the market place.

Operating Expenses

Research and development expense was \$118,000 and \$193,000 for the three and six months ended June 30, 1992 versus \$312,000 and \$467,000 for the three and six months ended June 30, 1991. The lower research and development expense for the quarter and six months was in part the result of software development costs of \$61,000 and \$118,000, respectively, which were capitalized. These costs were associated with several new software products which the Company announced in June. Also contributing to the lower research and development expense was a greater level of engineering services that was contract related, as opposed to internal Company development, and thus was included in cost of revenue.

Marketing expense was \$142,000 and \$274,000 for the three and six months ended June 30, 1992 as compared to \$142,000 and \$239,000 a year ago. There was no change in total marketing expense in second quarter 1992 as compared to 1991. The six months 1992 total reflects increased spending from 1991 levels relating to additional personnel. Since June 1992, the Company has added some additional sales personnel to follow-up on a recent increase in number of opportunities. These additions will result in higher level of marketing and sales expense in the second half of 1992.

General and administrative expense for the three and six months ended June 30, 1992 decreased to \$147,000 and \$293,000 from \$167,000 and \$330,000 for the three and six months ended June 30, 1991. The decrease in general and administrative expense was due primarily to an accrual for bonuses in the second quarter and first six months 1991 based on relatively higher earnings in the corresponding periods.

Interest and Other Income

Interest and other income was \$42,000 and \$96,000 for the three and six months ended June 30, 1992 as compared to \$263,000 and \$283,000 for the three and six months ended June 30, 1991. The 1991 totals include a net benefit of approximately \$250,000 in second quarter 1991 relating to the favorable settlement of a claim regarding an investment loss in 1987. Before the effect of this benefit, interest income was greater than the prior year due to the increased return on the higher cash balances in 1992 versus 1991.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 1992, the Company's cash and cash equivalents totaled \$4,569,000 as compared to \$4,724,000 at December 31, 1991. At June 30, 1992, the Company's current ratio was approximately 7 to 1. The Company has no commercial lending facilities.

During the first six months of 1992, the Company used cash of \$138,000 in operating activities and \$288,000 in investing activities. The use of cash was offset partially by \$271,000 provided by financing activities. For the first six months of 1991, the Company generated \$337,000 from operating activities which was offset by \$62,000 in investing activities and \$141,000 primarily relating to principal payments under capital lease obligations and a note payable.

Over the past two years, the Company has shown the capability to achieve profitable operations on a sustained basis. Moreover, the Company believes that with the demonstrated profitability and the additional equity provided by the unit offering completed in 1991, not only does the Company have greater financial flexibility and safety through increased liquidity, but also the resources to attract potential customers concerned with the ability of the Company to provide long-term product support. The Company believes that its current working capital and funds generated from operations will be adequate to enable the Company to continue on-going operations and to meet its currently expected needs for working capital and capital expenditures over at least the next twelve months.

In the past, the Company has generally limited the number of contracts sought from customers requiring substantial bonds or deposits; however, such bonds or deposits are often required by state and

local governments, and occasionally by other types of potential customers. Bond or deposit amounts required are generally a percentage of the total contract price. Such bonds or deposits generally must remain in place from the award of the contract until acceptance of the work performed, which in the absence of a dispute typically occurs within six to nine months after award of the contract. The Company does not expect that the posting of such bonds or deposits in the future will have a material adverse effect on the Company's ability to meet its needs for liquidity and working capital.

The Company anticipates that it will maintain its capital expenditures at a level consistent with past levels. Although there can be no assurance that the Company will experience further growth in revenues, management anticipates that additional revenue will increase the Company's working capital needs. In addition, as new opportunities arise, the Company expects to expand its technical and marketing staffs.

Net Operating Loss Tax Carryforwards

As of December 31, 1991, the Company had a net operating loss carryforward ("NOL") for Federal income tax purposes of \$16,400,000. In addition, the Company generated but has not used research and investment tax credits for Federal income tax purposes of approximately \$700,000. Under the Internal Revenue Code of 1986, as amended (the "Code"), the Company generally would be entitled to reduce its future Federal income tax liabilities by carrying unused NOL forward for a period of 15 years to offset future taxable income earned, and by carrying unused tax credits forward for a period of 15 years to offset future income taxes. The Company's ability to utilize any NOL and credit carryforwards in future years may be restricted, however, in the event the Company undergoes an "ownership change" as defined in the Code. In the event of an ownership change, the amount of NOL attributable to the period prior to the ownership change that may be used to offset taxable income in any year thereafter generally may not exceed the fair market value of the Company immediately before the ownership change (subject to certain adjustments) multiplied by the applicable long-term, tax-exempt rate announced by the Internal Revenue Service in effect for the date of the ownership change. A further limitation would apply to restrict the amount of credit carryforwards that might be used in any year after the ownership change. As a result of these limitations, in the event of an ownership change, the Company's ability to use its NOL and credit carryforwards in future years may be delayed and, to the extent the carryforward amounts cannot be fully utilized under these limitations within the carryforward periods, these carryforwards will be lost. Accordingly, the Company may be required to pay more Federal income taxes or to pay such taxes sooner than if the use of its NOL and credit carryforwards were not restricted.

The Company does not believe it has undergone an ownership change since 1987. Nonetheless, additional issuances of equity securities by the Company or the transfer of outstanding equity securities by shareholders could result in an ownership change, thereby subjecting the Company to the limitations described above.

PART II. OTHER INFORMATION

Item 4 - Submission of Matters to a Vote of Security Holders:

The Annual Meeting of Shareholders was held June 12, 1992. At the meeting, the shareholders approved a proposal to amend the Company's 1987 Stock Option Plan to reflect certain changes in Rule 16b-3 under the Securities Exchange Act of 1934 and to delete certain restrictions on granting of options and the exercising of options by Directors. The proposal was approved with 7,614,527 proxies voting yes, 484,000 voting no, and 145,757 abstaining.

In addition, at the meeting, the following individuals were elected as directors who will hold office until the next annual meeting: Walter F. Bauer, Robert T. Bruce, Roger H. Erickson, Michael J. McGovern, William C. Silbert, and Larry D. Unruh.

Item 6 - Exhibits and Reports on Form 8-K:

- (a) Exhibits - See Exhibit Index on Page 11.
- (b) There were no reports on Form 8-K filed for the three months ended June 30, 1992.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ALPHAREL, INC.

By: /s/Roger H. Erickson
Roger H. Erickson
President and Chief Executive Officer

By: /s/John W. Low
John W. Low
Chief Financial Officer

Dated: August 12, 1992

EXHIBIT INDEX

Exhibit

Page Number

11

Statement Re Computation of
Net Income Per Share

12

ALPHAREL, INC.

STATEMENT RE COMPUTATION OF NET INCOME PER SHARE

(Unaudited)

(In thousands except per share data)

	For three months ended June 30,		For six months ended June 30,	
	1992	1991	1992	1991
Net income per consolidated financial statements	\$ 61	\$ 403	\$ 122	\$ 659
Primary net income per share:				
Weighted average common shares	11,343	9,351	11,313	9,301
Common stock equivalents:				
Common stock options	526	694	585	716
Common stock warrants	-	-	1	-
Weighted average shares outstanding	<u>11,869</u>	<u>10,045</u>	<u>11,899</u>	<u>10,017</u>
Fully diluted net income per share:				
Weighted average common shares	11,343	9,351	11,313	9,301
Common stock equivalents:				
Common stock options	526	694	585	716
Common stock warrants	-	-	1	-
Weighted average shares outstanding	<u>11,869</u>	<u>10,045</u>	<u>11,899</u>	<u>10,017</u>
Net income per share:				
Primary	\$ <u>.01</u>	\$ <u>.04</u>	\$ <u>.01</u>	\$ <u>.07</u>
Fully diluted	\$ <u>.01</u>	\$ <u>.04</u>	\$ <u>.01</u>	\$ <u>.07</u>